Economic Trends

Exports and housing lift Alberta's economy

With only one quarter remaining, 2014 is shaping up to be another strong year for Alberta's economy. Indicators show that the economy is getting a boost from a number of sources. Two standout performers have been housing starts and exports, which have posted double digit growth so far this year. This month's inFocus provides an overview of developments in rail transportation for crude products.

Household Sector

Record international migration

Alberta led all provinces in population growth for the fourteenth straight quarter. At 2.9% year-over-year (y/y), second quarter growth was nearly triple the national average. The province added about 35,000 people, including around 12,700 immigrants, the highest level on record, and over 13,000 net interprovincial migrants. Due to historical revisions, Alberta population growth for the 2013 census year is now 3.0%, down from the previous estimate of 3.5%. This was mainly due to lower estimated net interprovincial migration.

Key Indicators — Seasonally adjusted unless otherwise indicated.

Indicator	Latest Month	Value	Change year-over-year (y/y)
Employment (thousands)	August	2,260	+1.7%
Unemployment Rate	August	4.9%	+0.1 p.p.
CPI Inflation (unadjusted)	August	2.6%	+1.2 p.p.
Retail Sales	July	$6.6 B	+8.9%
Housing Starts (annualized)	August	41,117	+40.0%
Rigs Drilling (unadjusted)	August	254	+6.5%
Manufacturing Shipments	July	$6.9 B	+16.1%
Exports (unadjusted)	July	$10.4 B	+19.1%

Source: Statistics Canada, CAODC, CMHC, p.p.= percentage points.

Jobs still need filling

Despite the inflow of workers, the number of job vacancies has accelerated over the first half of 2014. The job vacancy rate has been persistently high, averaging 2.4% since January, compared with 1.5% for Canada. However, growth in the job vacancy rate has been contained in recent months, as the number of occupied positions has kept pace with vacancies. Alberta's employment growth has led all provinces, at 3.2% year-to-date (YTD), although there have been job losses in each of the last two months and year-over-year growth has recently trended lower.

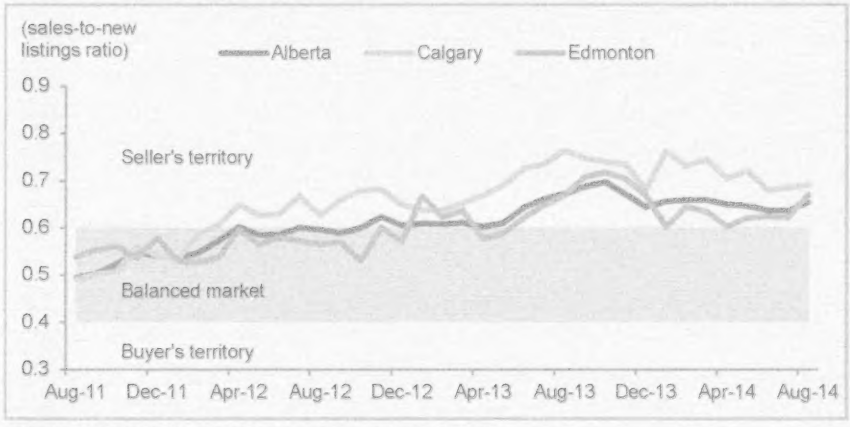
Housing market picks up

The Alberta housing market has been persistently strong, with sales up 8.8% through eight months of the year. Strong sales have kept the sales-to-new listings (SNL) ratio at an average of 0.65 since January, firmly in seller's territory (Chart 1). The SNL ratios for Edmonton and Calgary have been converging as activity in Edmonton has picked up, although Calgary has seen much stronger price increases. The two cities account for over 70% of Alberta's resale market. Housing starts have posted solid growth, up 12.2% so far this year, bolstered by strong in-migration.

Shelter keeps inflation elevated

Alberta inflation held steady at 2.6% in August, with year-to-date inflation at 2.7%. The driver of Alberta's

Chart 1: Alberta stays in a seller's housing market
Sales-to-New Listings Ratio



Source: Canadian Real Estate Association (CREA)

inflation continues to be shelter costs. Year-to-date shelter costs are up 4.1%. The owned accommodation component has been pushed up by homeowners' home and mortgage insurance, which is up 14.2% so far this year. The volatile energy component has added to shelter costs this year.

Alberta Business Sector

Export gains go beyond energy

Alberta exports have seen phenomenal growth this year, posting double-digit year-over-year growth in every month, and are up 21.2% YTD. Energy exports continue to lead, but other sectors are also contributing. In response to an expanding US housing sector, Alberta lumber producers have shifted from domestic to international supply. Exports of wood products to the US have picked up 41.1% YTD, compared with 32.1% to all destinations. In addition, after several months of negative growth, farm product exports turned a corner in June, and are now up 16.2% YTD.

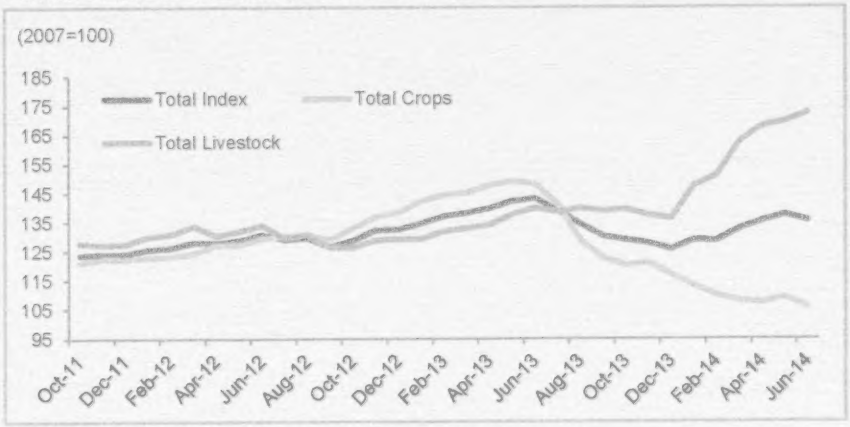
New record in manufacturing

Alberta manufacturing shipments surpassed their pre-recession peak in June, hitting almost $7.0 billion, before pulling back slightly in July. Sales of manufacturing goods have expanded 9.6% YTD. Growth has been broad-based across most sectors. Food products and petroleum & coal have benefited from higher production and prices. Machinery and equipment products continue to expand, up 10.7% YTD. Chemical manufacturing picked up again after maintenance and expansion at a major plant through May and early June, with sales up 5.2% YTD.

Light-Heavy differential tightens

Heavy oil producers in Alberta have received a boost recently. The differential between North America's benchmark WTI price and Alberta's heavy benchmark WCS is currently hovering around US$14.50/bbl, the narrowest light-heavy (LH) differential in over a year. Heavy oil prices have been helped by linefill activity, growth in mid-west heavy oil processing capacity, and increased crude-by-rail shipments that have reduced bottlenecks. Support from the tightening LH differential has been offset somewhat by lower WTI prices.

Chart 2: Diverging movements in agriculture prices
Alberta Farm Product Price Index 2007=100



Sources: Statistics Canada

Farm prices diverge

Production trends have contributed to a growing divide in the prices farmers are receiving for their crops and livestock (Chart 2). Crop prices have been falling, due in part to lingering inventories from last year's bumper crops. On the other hand, shrinking North American cattle and hogs supplies have been driving livestock prices higher. This has supported growth in food manufacturing and contributed to higher consumer prices for meat.

Outside Alberta

Exports boost Canadian growth

Canada's economy has gained some momentum, as second quarter GDP growth came in at 3.1%, up from a disappointing first quarter. Exports, which have struggled to gain traction since the recession, posted a large, broad-based jump in the second quarter. Household consumption and business investment also contributed to the strong reading. Despite the pickup, labor markets remain weak, with little job growth recorded in the last year. The Bank of Canada (BoC) is maintaining the overnight rate at 1%. This accommodative stance will provid further support to exporters that are already benefiting from a resurgent US economy and a weaker Canadian dollar.

Diverging policy in the US and EU

Economic conditions in North America and the Eurozone are diverging, leading central banks in different directions. The US economy rebounded sharply in the second quarter, and the US Federal Reserve signaled an end to its asset purchases in October if labour markets improve further. However, the FOMC is widely expected to leave the fed funds rate between 0% to 0.25% as long as labour markets remain weak and inflation stays low.

Meanwhile, the Eurozone's economy has stagnated, and there are ongoing concerns about deflation. The European Central Bank recently lowered its target interest rate by 10 basis points to 0.05%. The ECB has also announced that it will begin two asset purchase programs next month.

Contact

Catherine Rothrock 780.427.2758

inFocus

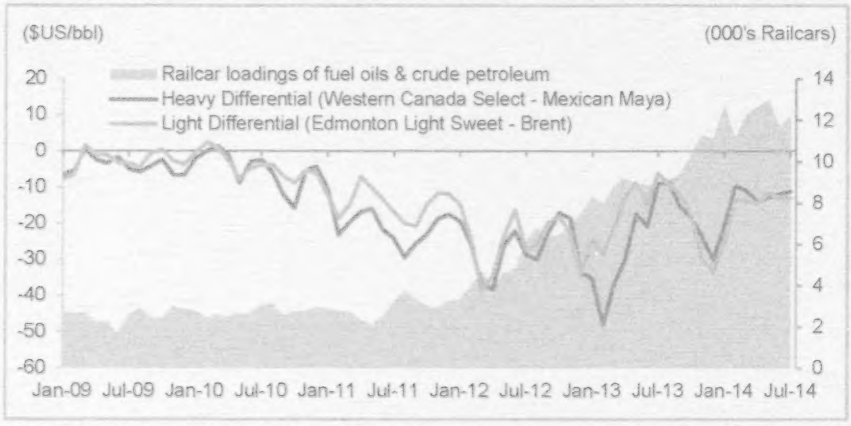
The emergence of crude by rail

Given the strong outlook for crude production, pipeline bottlenecks remain a concern for Alberta oil producers. Rail has emerged as a quickly scalable, though more expensive, method to get Alberta crude to market. This infocus explores the growing significance of crude by rail, the destination of these rail movements, and what investment and construction plans indicate about the future.

Pipeline constraints encourage investment in rail

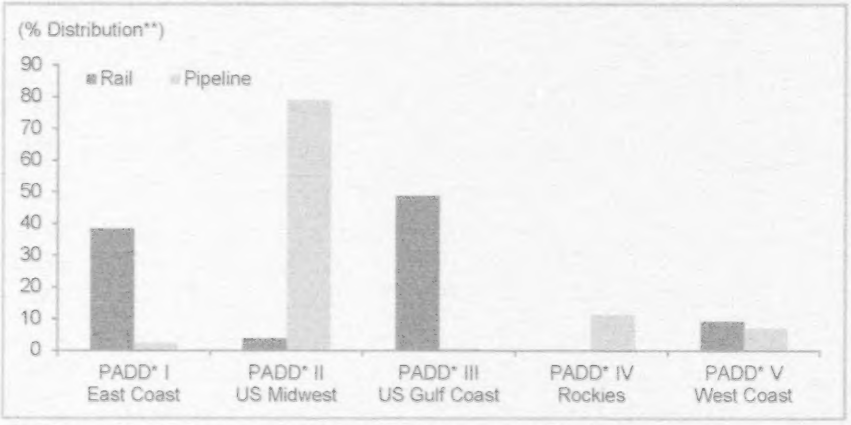
In recent years, Alberta crudes have traded at deep price discounts relative to North American and global oil price benchmarks. This reflects constraints to pipeline capacity in the face of rising North American production, resulting in oversupply in Alberta's main market, the US Midwest (PADD II), as well as increased price volatility from pipeline outages. New and expanded pipelines have helped clear inventories at Cushing, Oklahoma, but bottlenecks still exist in Alberta. Large price discounts have encouraged investment in rail capacity, since rail allows producers to access higher prices in alternative markets. As a result, crude-by-rail volumes have more than tripled over the last two years (Chart 1). This has helped to reduce the crude bottleneck in Alberta and support prices for Canadian crudes.

Chart 1. Rail movements pick up as price discounts widen
Alberta oil prices relative to benchmarks and Western Canada rail movements



Sources: Statistics Canada and Alberta Energy

Chart 2. Rail reaches markets not as accessible by pipeline
Alberta's crude exported by mode and final US destination in 2013



Source: Statistics Canada and Treasury Board and Finance Calculations
* US Petroleum Administration for Defense District (PADD)
** Percentage based on total cubic metres delivered

Expanding the transport network

Statistics Canada reports that investment in support activities for transportation, which includes construction of new rail loading facilities, has expanded 78.5% since 2010, from $1.6 billion nationally to nearly $2.9 billion expected in 2014. Much of this comes from the construction of an estimated six new crude-by-rail loading facilities in Alberta. In addition, most of the operating terminals in Alberta will be undergoing expansions over the next two years, according to the Canadian Association of Petroleum Producers (CAPP). This will balloon Western Canada's rail transportation capacity from 300,000 barrels per day in 2013 to 1.0 million by the end of 2015. CAPP anticipates capacity utilization of these facilties will reach about 50% by the end of 2016.

Flexible mobility, but a higher cost

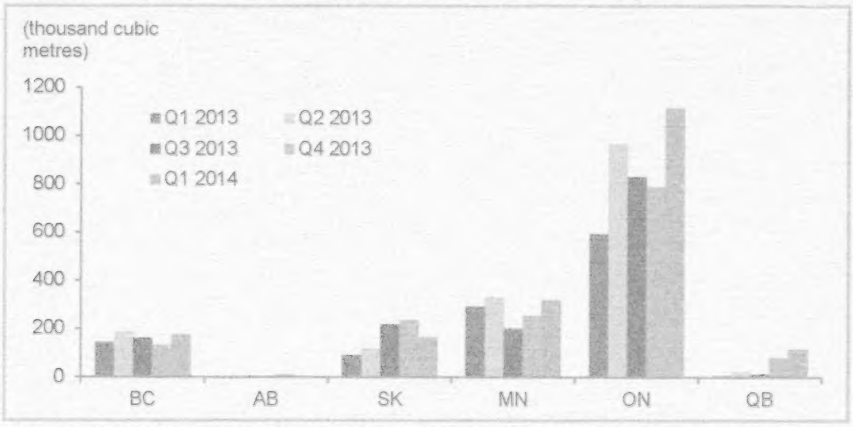
Crude-by-rail provides access to alternative markets because, unlike pipelines, rail has flexible delivery alternatives. This has enabled Alberta producers to ship away from

bottlenecked PADD II into regions where demand for Alberta crude, particularly heavy crude, is strong and there is little or no pipeline access.

The main destinations for Alberta's crude transported by rail are PADD I (US East Coast) and III (US Gulf Coast) (Chart 2). These two regions have access to tide water and provide better linkages to international markets, which enables producers to access prices that better reflect the value of their crude. Rail has also provided greater access to Eastern Canada. In fact, comparatively little crude moves south directly from Alberta by rail. Instead, Alberta's crude crosses the country to reach its destination in the United States, with nearly 60% crossing the border in Ontario (Chart 3).

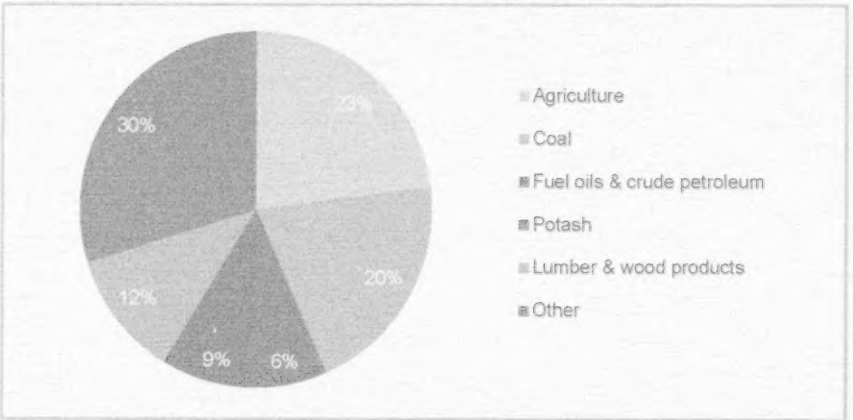
Despite the flexibility of rail, the per barrel cost to transport a barrel of oil by rail is higher than shipments by pipeline. The National Energy Board (NEB) estimates that pipeline transportation costs between $5.00/bbl and $9.55/bbl, depending on the destination. By comparison, CAPP estimates costs for transporting crude-by-rail between $9.38/bbl to $22.61/barrel, with the West Coast as a lower cost destination, and the East Coast on the higher end. This higher cost is passed to producers through lower netbacks. Although it costs more, the market access that rail provides has promoted further investment in rail capacity.

Chart 3. Alberta ships crude through other provinces
Alberta crude-by-rail exports by province of border crossing



Source: Statistics Canada and Treasury Board and Finance Calculations

Chart 4. Crude by rail - a small portion of railcar movements
2013 Western Canadian railcar movements by product share



Source: Statistics Canada

A small share of rail movements

Crude products shipped by rail represent the fastest growing segments of railcar movements, but only a small fraction of overall movements. In 2013, the number of railcars moving crude products in Western Canada expanded 71.6%, much higher than the 4.7% average increase. However, crude movements represented only 6.3% of Western Canadian railcar movements, and 5.0% nationally. This makes crude product movements slightly less than potash shipments from Saskatchewan, and significantly less than agricultural cars (Chart 4). While a comparatively small segment, the rapid increase in crude moving by rail adds pressure to transportation infrastructure, increasing demand for rail crews and locomotives.

Pipelines remain vital

Despite the rapid growth of crude by rail, pipelines remain the dominant method to transport oil from Alberta. Almost 20 times more oil was moved by pipeline from Alberta than by train in 2013. Even with continued investment in rail facilities, this trend is not likely to change. Several new pipeline projects are currently being considered by the National Energy Board, while other existing projects are expanding capacity. The lower per barrel cost in transporting crude by pipeline makes it an attractive option for producers. While crude by rail has filled a logistics gap in the face of delays in pipeline developments, rising crude production will require the continued development of pipelines.

Contact

Warren Kirkland 780.427.8845